

**Can undue insistence on conformity with procedural due process  
create an impediment for economically inferior parties in attaining  
arbitral justice?**

Author: Akerele, Michael

University of Helsinki

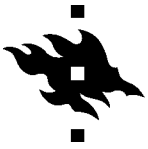
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Tiivistelmä – Referat – Abstract  <p>When parties become unable to pay for the costs of arbitration, they sometimes seek to resort to litigation in national courts. In such circumstances, UK courts, in reference to the UK Arbitration Act, have held that impecuniosity of a party would not invalidate the agreement to arbitrate and impecunious parties could thus not be allowed to resort to litigation while there is a valid arbitration agreement.</p> <p>Research in this thesis found, in light of recent US courts decisions, that an economically superior party could purposely make arbitration expensive and consequently unaffordable for an economically inferior party by insisting on undue conformity with the requirements of procedural due process. When issue of impecuniosity is raised by a party who seeks to resort to litigation and a counterparty seeks to compel arbitration, the approach of the US courts is that the party who seeks to compel arbitration could either pay for the costs of arbitration or the impecunious party should be allowed to resort to litigation in the national court.</p> <p>This thesis suggests that in order not to foreclose economically inferior parties from obtaining justice because of impecuniosity which might be unscrupulously occasioned by economically superior parties during the course of arbitration, the UK courts should adopt similar approach taken by the US courts in some cases.</p>			
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## **Abbreviations**

AAA – America Arbitration Association

CCP – Civil Procedure Code

ECHR – European Convention on Human Rights

EU – European Union

FAA – Federation Arbitration Act

IAS – International Arbitration Survey

ICC – International Chamber of Commerce

LCIA – London Court of International Arbitration

PwC – PricewaterhouseCoopers

QMUL – Queen Mary University of London

SCC – Stockholm Chamber of Commerce

SIA – School of International Arbitration

UK – United Kingdom

UNCITRAL – United Nations Commission on International Trade and Law

US – United States

USD – United States Dollar

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# 1 Introduction

## 1.1 Background and purpose of study

When legal proceedings are brought against a party to an arbitration agreement, section 9 of the UK Arbitration Act<sup>1</sup> requires courts to stay proceedings, except in given circumstances. In view of this, UK courts are often reluctant to entertain jurisdiction where the parties have a valid agreement to settle their disputes by arbitration. There are peculiar cases however, where parties, despite having agreed to settle disputes by arbitration, have raised the issue of impecuniosity as an impediment to resolving their disputes by arbitration. In such cases, UK courts, with reference to the Arbitration Act 1996, have held that impecuniosity of a party would not invalidate an agreement to arbitrate and have thus declined jurisdiction. Recent cases in the US courts however, revealed that parties could tactfully increase arbitration costs by insisting on undue conformity with the requirements of procedural due process.

Proponents of arbitration often argue that it is a cheap method of dispute resolution as opposed to litigation. Such arguments are usually based on the assumption that the proceedings are conducted within time and cost schedule. Arbitration costs, however, could be increased by additional expenses resulting from undue conformity with the requirements of procedural due process. The Californian Court of Appeal in *Weiler*<sup>2</sup> thus observed that:

Plaintiff was ordered to arbitrate her claims and she proceeded to do so. But after nearly three years of arbitration, during which defendants supposedly “engaged in a scorched earth policy and . . . ‘piled on’ the onerous costs of arbitration[,]” she claims to be unable to continue to afford to arbitrate.<sup>3</sup>

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1 Arbitration Act 1996.

2 2018 WL 2011048 (Cal. Ct. App. 4th Dist. no. G053953 (Apr. 30, 2018).

3 *ibid.*

Many objections raised during arbitral proceedings are usually predicated on conformity with due process requirements and deciding on conformity places an onerous duty on arbitrators. There are usually “rule-free zones” in which the arbitral tribunal must respond to ad hoc procedural moves by the parties and in such situations, arbitrators are faced with the difficult task of determining the motives of the parties for confronting them with such procedural maneuvers or requests.<sup>4</sup> ‘In some scenarios, this task is relatively easy to complete because the parties’ procedural moves are either clearly legitimate exercises of their procedural rights, or “guerrilla tactics”, obviously motivated solely by the desire to obstruct the arbitral process’.<sup>5</sup>

The SIA 2015 survey found that one of the issues causing delays in arbitration proceedings is the ‘reluctance by tribunals to act decisively in certain situations for fear of the arbitral award being challenged on the basis of a party not having had the chance to present its case fully.’<sup>6</sup> This phenomenon, according to the survey was dubbed ‘due process paranoia’ by one of the interviewees in the survey. Respondents in the survey described situations where deadlines were extended several times, ‘new evidence was admitted late in the process or other disruptive behaviour by counsel was condoned due to what was perceived to be a concern by the tribunal that the award would otherwise be vulnerable to challenge.’<sup>7</sup> The survey found that arbitrators also identified this phenomenon as both problematic and commonplace and many revealed in interviews that this concern has influence on decisions they have made when sitting as arbitrator.<sup>8</sup>

In recent past, there have been some studies on how impecuniosity of parties could necessitate the invalidation of an arbitration clause.<sup>9</sup> Such studies usually focus on the assumption that the

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4 Klaus Peter Berger and J. Ole Jensen, 'Due process paranoia and the procedural judgment rule: a safe harbor for procedural management decisions by international arbitrators', in João Bosco Lee and Daniel de Andrade Levy (eds), *Revista Brasileira de Arbitragem*, (© Comitê Brasileiro de Arbitragem CBAr & IOB; Kluwer Law International 2017, Volume XIV Issue 54) pp. 73 – 94.

5 *ibid* 75.

6 QMUL, ‘2015 International Arbitration Survey: Improvements and Innovations in International Arbitration’, 2015 <[http://www.arbitration.qmul.ac.uk/media/arbitration/docs/2015\\_International\\_Arbitration\\_Survey.pdf](http://www.arbitration.qmul.ac.uk/media/arbitration/docs/2015_International_Arbitration_Survey.pdf)> accessed 28 February 2019.

7 *ibid*.

8 *ibid*.

9 Deutsche Institution für Schiedsgerichtsbarkeit, *Financial Capacity of the Parties: A Condition for the Validity of Arbitration Agreements?*, Schriftenreihe Der August-Maria-Berges-Stiftung Für Arbitrales Recht 16 (Frankfurt am Main: Peter Lang, 2004).

impecuniosity of the party arose before the commencement of arbitration. This thesis however, in light of recent court decisions, goes further, by examining how impecuniosity which arose as a result of undue insistence on conformity with the requirement of procedural due process during arbitration proceedings could create an impediment to the prosecution of a party's case. The study analyses how undue conformity with the requirements of due process occasion additional costs in arbitration proceedings and consequently weaken the financial ability of an economically inferior party.

It is argued that undue insistence on conformity with the requirements of procedural due process in arbitral proceedings could increase the costs involved in the proceedings and consequently constitute an impediment to the prosecution of the case of an economically inferior party.

## **1.2 Scope of study**

The primary focus of this study is on commercial arbitration proceedings in the United Kingdom. United Kingdom in this context, refers only to England and Wales or Northern Ireland because the UK Arbitration Act 1996 does not apply to Scotland which is also a UK jurisdiction. By way of comparative analysis, decisions in US cases shall also be examined. The study assumes that third party fundings are not available to the parties.

This thesis raises three research questions, to wit:

1. Can costs resulting from conformity with the requirements of procedural due process increase the costs of arbitration?
2. Can a party in arbitration proceedings tactfully make an opposing party impecunious by insisting on undue conformity with the requirements of procedural due process?
3. Should a party be allowed to resort to litigation if it becomes impossible to obtain arbitral justice because of impecuniosity?

### **1.3 Methodology**

This thesis utilises legal-dogmatic research. The thesis begins with an analysis of how activities centered around conformity with the requirements of procedural due process could affect the financial ability of an economically inferior party. This is followed by a comparative analysis of case law to examine how the courts deal with the issue of impecuniosity of a party as an impediment to attainment of justice in the UK in comparison with how the matter is approached by the US courts.

Due to the usual confidential nature of arbitral proceedings, many arbitral awards are unpublished. Although published awards lack formal precedential value and are only binding on the parties to whom they are rendered, the awards ‘constitute highly persuasive forms of authority, particularly with respect to procedural matters that are not typically discussed in judicial opinions.’<sup>10</sup> Scholarly works from leading arbitration practitioners with practical experience in international arbitration may be referred to where necessary to fill in the gaps.<sup>11</sup>

### **1.4 Thesis outline**

This thesis consists of 5 chapters.

The current chapter is the introductory chapter.

Chapter 2 provides an analysis of the financial impact of undue conformity with the requirements of procedural due process on the financial ability of an economically inferior party in an arbitration proceeding. The chapter begins with a brief analysis of arbitration fees and other expenses of arbitration followed by an examination of the relevance of procedural due process and the impact of undue conformity with same on the financial stamina of an economically inferior party.

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10 S.I. Strong, Research in International Commercial Arbitration: Special Skills, Special Sources, 20 Am. Rev. Int'l Arb. 119 (2009).

11 *ibid* 150.

Chapter 3 examines how UK courts deal with the issue of impecuniosity of a party in comparison to the approach in the US. Relying on recent decisions of the US courts, the chapter makes a theoretical analysis of how an economically superior party could purposely insist on undue conformity with the requirements of procedural due process in order to frustrate an economically inferior party out of an arbitration proceeding.

Chapter 4 discusses some ways to mitigate the financial problems which is usually occasioned to economically inferior parties as a result of undue insistence on procedural due process conformity by economically superior parties.

Chapter 5 is the concluding chapter. The chapter emphasises the plights of economically inferior parties in obtaining justice when they become unable to afford the costs of arbitration and it is suggested that the UK should adopt similar approach taken by the US courts.

## **2 Financial impact of undue conformity with procedural due process on economically inferior parties**

### **2.1 Arbitration fees and other costs**

Section 59 – 65 of the Arbitration Act<sup>12</sup> govern costs in arbitrations seated in England and Wales or Northern Ireland and the provisions apply unless the parties agreed otherwise. Costs according to section 59 includes:

- (a) The arbitrators' fees and expenses;
- (b) The fees and expenses of any arbitral institution concerned;
- (c) The legal or other costs of the parties.

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<sup>12</sup> Arbitration Act 1996.

(d) costs of or incidental to any proceedings to determine the amount of the recoverable costs of the arbitration

The provisions of section 59 to 65<sup>13</sup> are not mandatory so parties can thus agree to the contrary. The provisions of the rules of arbitral institutions in regard to costs may apply if parties had elected to be governed by such rules. Actual costs of arbitration are usually decided by arbitral institutions and usually exclude external legal costs.

In 2017, the London Court of International Arbitration published a report<sup>14</sup> on the average cost and duration of its arbitration as an update to an earlier report published in 2015 and other leading arbitral institutions have since followed suit. The report was based on 224 cases administered under the LCIA Rules that reached a final award between 1 January 2013 and 31 December 2016. The report established that, an average LCIA arbitration lasts 16 months and costs USD 97,000.

The Hong Kong International Arbitration Centre, Stockholm Chamber of Commerce and the Singapore International Arbitration Centre among other leading arbitral institutions, also produced similar reports<sup>15</sup> on costs and duration of their arbitral proceedings. According to the said reports, there is no specific timeframe or cost of the arbitration proceedings. The duration and cost will be affected by the particular circumstances of each individual case. The more complex the case the longer it is likely to take and the higher the cost. The proceedings of the LCIA, HKIAC, and SCC take more than a year and longer in some cases.

The estimated costs in the reports of LCIA, HKIAC and SIAC only reflected administrative fees and fees paid to arbitrators which together constitutes only a small portion (about 20%) of the cost of the arbitral proceedings according to the reports: Although, SCC in its Report, gave an estimate

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<sup>13</sup> *ibid.*

<sup>14</sup> London Court of International Arbitration, 'Facts and Figures – Costs and Duration: 2013 – 2016' (2017) <<https://www.lcia.org/News/lcia-releases-updated-costs-and-duration-analysis.aspx>> accessed 24 February 2019.

<sup>15</sup> Hong Kong International Arbitration Centre, 'Average Costs and Duration' <<http://www.hkiac.org/content/costs-duration>> accessed 24 February 2019; Stockholm Chamber of Commerce, 'Costs of arbitration and apportionment of costs under the SCC Rules' (2016) <[https://sccinstitute.com/media/93440/costs-of-arbitration\\_scc-report\\_2016.pdf](https://sccinstitute.com/media/93440/costs-of-arbitration_scc-report_2016.pdf)> accessed 24 February 2019; Singapore International Arbitration Centre, 'Costs and Duration Study' (2016).



of costs claimed by parties for legal representation, the ‘report excludes costs incurred for expenses by the parties, counsel, the tribunal and the SCC’.<sup>16</sup>

The American Arbitration Association likewise stated that other than Administrative fees and arbitrator compensation and expenses, each party would incur additional costs to conduct their case in arbitration just as they would in court. Such costs according to the AAA might include ‘attorneys’ fees, costs for expert witnesses, costs to have witnesses travel to the arbitration, costs for copying and presenting exhibits, etc.’<sup>17</sup>

A 2011 survey by the Chartered Institute of Arbitrators found that ‘74% of party costs were spent on external legal costs (including where applicable barristers’ fees), ...’.<sup>18</sup> Of the 74% of costs, ‘... parties spent 19% on the pre-commencement/commencement of the arbitration, 25% on exchange of pleadings, 5% on discovery, 14% on fact and expert witnesses, and the remaining 37% on the hearing’<sup>19</sup>.

The foregoing analysis of arbitration fees and costs show that external legal costs constitutes a major part of the costs of arbitration. Such costs are usually excluded from the arbitration costs in the determination of costs in arbitral awards. For instance, Article 28.1 of the LCIA rules provides that ‘[t]he costs of the arbitration other than the legal or other expenses incurred by the parties themselves (the “Arbitration Costs”) shall be determined by the LCIA Court in accordance with the Schedule of Costs ...’<sup>20</sup> This shows that increase in external legal costs in arbitral proceedings is more likely to be to the detriment of an economically inferior party.

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16 Stockholm Chamber of Commerce, ‘Costs of arbitration and apportionment of costs under the SCC Rules’ (2016) <[https://sccinstitute.com/media/93440/costs-of-arbitration\\_scc-report\\_2016.pdf](https://sccinstitute.com/media/93440/costs-of-arbitration_scc-report_2016.pdf)> accessed 24 February 2019.

17 AAA, Costs of Arbitration <[https://www.adr.org/sites/default/files/document\\_repository/AAA228\\_Costs\\_of\\_Arbitration.pdf](https://www.adr.org/sites/default/files/document_repository/AAA228_Costs_of_Arbitration.pdf)> accessed 28 May, 2019.

18 Chartered Institute of Arbitrators, ‘CiArb Costs of International Arbitration Survey 2011’ <<https://www.international-arbitration-attorney.com/wp-content/uploads/2017/01/CiArb-Cost-of-International-Arbitration-Survey.pdf>> accessed 26 February 2011.

19 *ibid.*

20 London Court of International Arbitration ‘Arbitration Rules’ (2014) <[http://www.lcia.org/Dispute\\_Resolution\\_Services/lcia-arbitration-rules-2014.aspx](http://www.lcia.org/Dispute_Resolution_Services/lcia-arbitration-rules-2014.aspx)> accessed 1 May 2017.

In many cases, economically inferior parties inevitably find themselves unable to keep up with the expenses needed to fully prosecute their claims. In *Michael Jonathan Christopher Oldham v QBE Insurance (Europe) Limited*,<sup>21</sup> for instance, the claimant, who had been a party in an underlying arbitration proceedings, challenged two arbitral awards ordering him to pay costs. The challenge was made under section 68 of the Arbitration Act 1996 on the grounds that he was not given a reasonable opportunity to address argument in respect of costs. He later sought an adjournment during court proceedings to enable him to seek the representation of another counsel after his previous counsel dropped the brief for non payment.

## 2.2 Relevance of procedural due process

The aim of procedural due process in arbitration is ‘to ensure that the parties are treated with equality and are given a fair hearing, with a proper opportunity to present their respective cases’.<sup>22</sup> The requirement of due process is rooted in the principles of natural justice. Natural justice is a revered concept of law in many countries and its precise origin is difficult to trace. In regard to the origin of natural justice and its essence, Smith observed thus:

‘That no man is to be judged unheard was a precept known to the Greeks, inscribed in ancient times upon images in places where justice was administered, proclaimed in Seneca's *Medea*, enshrined in the Scriptures, embodied in Germanic proverbs, ascribed in the Year Books to the law of nature, asserted by Coke to be a principle of divine justice, and traced by an eighteenth-century judge to the events in the Garden of Eden. The historical and philosophical foundations of the English concept of "natural" justice may be insecure; it is not the less worthy of preservation.’<sup>23</sup>

Article 6 (1) of the European Convention on Human Rights provides that ‘In the determination of his civil rights and obligations or of any criminal charge against him, everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by

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21 [2017] EWHC 3045 (Comm).

22 Nigel Blackaby and others, *Redfern and Hunter on International Arbitration* (6<sup>th</sup> edn, OUP 2015), 586-587.

23 S.A. Smith, ‘Administrative Hearings in English Law’ (citations omitted).

law. ...'<sup>24</sup> However, according to English case law, by agreeing to arbitrate, parties will be deemed to have waived their right under Article 6 (1) of the ECHR.<sup>25</sup>

Arbitral institutions aim to make an award final without recourse to state courts. The LCIA Rules<sup>26</sup> for instance provides that 'the parties also waive irrevocably their right to any form of appeal, review, or recourse to any state court or other judicial authority insofar as such waiver may be validly made'. Even though most institutional rules include a provision on waiver of the right of recourse or appeal to state courts against arbitral awards, the arbitration law of many countries allow state court to interfere with arbitral awards in some circumstances. Such legislations seek to strike a balance between the finality of an award and the need to protect parties against unfair conduct in the arbitral process.

National courts in England are often reluctant to interfere with arbitral awards. There are however often circumstances upon which the court would interfere with an arbitral award. Such interference does not usually involve reviewing the facts of the case but an arbitral award may be set aside for non-conformity with the requirements of procedural due process. Section 1 (b) of the Arbitration Act<sup>27</sup> provides that 'the parties should be free to agree how their disputes are resolved, subject only to such safeguards as are necessary in the public interest'.

Section 33 (1) (b) of the Arbitration Act 1996 guarantees due process in arbitration. It provides as follows:

(1) The tribunal shall-

(a) act fairly and impartially as between the parties, giving each party a reasonable opportunity of putting his case and dealing with that of his opponent ...<sup>28</sup>

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24 Convention for the Protection of Human Rights and Fundamental Freedoms (European Convention on Human Rights, as amended) (ECHR).

25 *Amr Amin Hamza EL Nasharty v J. Sainsbury Plc*, [2007] EWHC 2618 (Comm).

26 London Court of International Arbitration 'Arbitration Rules' (2014), Art 26.9.

<[http://www.lcia.org/Dispute\\_Resolution\\_Services/lcia-arbitration-rules-2014.aspx](http://www.lcia.org/Dispute_Resolution_Services/lcia-arbitration-rules-2014.aspx)> accessed 1 May 2017.

27 Arbitration Act 1996.

28 *ibid*.

The Arbitration Act 1996 is applicable to England and Wales and Northern Ireland in the UK. Section 33 is mandatory by virtue of section 4 (1) of the Act i.e. it has effect notwithstanding any agreement to the contrary. By virtue of section 68,<sup>29</sup> an arbitral award may be challenged in court on ground of serious irregularity and breach of section 33 may constitute such serious irregularity.<sup>30</sup> Pursuant to section 68 (3), upon successful challenge, the award might be remitted back to the tribunal, set aside in whole or in part, or declared invalid in whole or in part.

In the US, many arbitration cases are administered under the rules of the American Arbitration Association. General provisions of the requirement of fair hearing in arbitration can be found under Rule 22 (a) and 32 (a) of the AAA<sup>31</sup> respectively provide as follows:

R-22. Pre-Hearing Exchange and Production of Information

(a) *Authority of arbitrator.* The arbitrator shall manage any necessary exchange of information among the parties with a view to achieving an efficient and economical resolution of the dispute, while at the same time promoting equality of treatment and safeguarding each party's opportunity to fairly present its claims and defenses.

R-32. Conduct of Proceedings

(a) The claimant shall present evidence to support its claim. The respondent shall then present evidence to support its defense. Witnesses for each party shall also submit to questions from the arbitrator and the adverse party. The arbitrator has the discretion to vary this procedure, provided that the parties are treated with equality and that each party has the right to be heard and is given a fair opportunity to present its case.

In the conduct of international arbitration proceedings, Article 20 (1) of the International Centre for Dispute Resolution's Rules of International Dispute Resolution Procedures<sup>32</sup> likewise provides that:

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<sup>29</sup> *ibid.*

<sup>30</sup> *ibid* s 33.

<sup>31</sup> American Arbitration Association Rules of Arbitration (2013).

<sup>32</sup> American Arbitration Association International Dispute Resolution Procedures (2014).

1. Subject to these Rules, the arbitral tribunal may conduct the arbitration in whatever manner it considers appropriate, provided that the parties are treated with equality and that each party has the right to be heard and is given a fair opportunity to present its case .

Enforceability of awards is one of the primary reasons why parties usually choose arbitration over litigation, it is thus imperative for both advocates and arbitrators to consider how any award emanating from an arbitral proceeding will be enforced.<sup>33</sup> The Convention on the Recognition and Enforcement of Foreign Arbitral Awards, also known as the New York Convention<sup>34</sup> is arguably the most influential legal regime in arbitration. The Convention is a treaty to which 159 countries are signatories. It allows the enforcement of arbitral awards obtained in a foreign state in a contracting state.<sup>35</sup> It also allows the enforcement of arbitral awards not considered as domestic in the contracting state where enforcement is sought.<sup>36</sup>

Article V of the convention provides circumstances under which courts of a contracting state may refuse to recognise and enforce an arbitral award for non-conformity with the requirements of due process. Conscious of the possibility that enforcement of an arbitral award might be sought in other countries pursuant to the New York Convention, arbitrators are usually mindful to ensure that their awards are able to withstand potential challenges under Article V.

In the spirit of compliance with the convention, the provisions of Article V of the New York Convention have been implemented in the arbitration laws of many contracting states. Likewise, in the interest of ensuring finality of arbitral awards, many arbitral institutions have implemented rules of arbitral proceedings which effectually enable conformity with Article V of the New York Convention. Other treaties like the European Convention on International Commercial Arbitration also implements substantial part of Article V of the New York Convention.<sup>37</sup>

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33 S.I. Strong, Research in International Commercial Arbitration: Special Skills, Special Sources, 20 Am. Rev. Int'l Arb. 119 (2009).

34 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958)

35 New York Convention (n 34) Art I.1.

36 New York Convention (n 34).

37 European Convention on International Commercial Arbitration (1961).

The United Nations Commission on International Trade Law Model Law and the UNCITRAL Arbitration Rules are also important legal frameworks in arbitration that aim to guarantee due process. The UNCITRAL Model Law has been adopted by many countries either in toto or through legislation largely based on the Model Law.<sup>38</sup> The UNCITRAL Arbitration Rules likewise have also been adopted in many arbitral institutions' rules. Although many arbitrations proceedings are usually conducted under the rules of an arbitration institution situate in such countries, it is not unusual for some arbitrations to be governed by other institutional rules. This could be by agreement of parties or by decision of an arbitral tribunal in some cases.

### **2.3 The problems with conformity**

Arbitral proceedings may suffer delays and consequently increased costs due to activities centered around conformity with the requirements of procedural due process. When people in the UK ('Brexiters') voted to leave the EU in 2016, only few, if any might have anticipated the difficulties that would be encountered in the break up process. With all the problems with securing a deal, the consequent delay and the dramatic events that followed in the UK parliament about the possibility of a second referendum, votes of no confidence, and repeated failure to secure a deal which subsequently led to the resignation of the UK Prime Minister, some have expressed regrets in voting to leave.

The Brexit situation is similar to situations where parties find themselves when the incidental expenses in arbitration proceedings start to rise beyond their financial means, same expenses they had tried to avoid in the first place by electing to settle disputes by arbitration. While parties are often advised that arbitration is a fast and cheap alternative dispute resolution to litigation, they are usually less informed or aware of the possible additional expenses that might be incurred during the course of arbitration proceeding.

Besides the advance of costs of arbitration, parties also often need to cover their attorneys' fees, and other expenses incurred during the proceedings.<sup>39</sup> An arbitration agreement, thus, imposes several financial burdens on the parties which can reach high amounts.<sup>40</sup> A 2013 survey conducted by the

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38 Jeff Waincymer, *Procedure and Evidence in International Arbitration*, (Kluwer 2012) 173.

39 Patricia Živković, 'Impecunious Parties in Arbitration: An Overview of European National Courts' Practice' *Croatian Arbitration Yearbook Volume 23 (2016)*.

40 *ibid*.

School of International Arbitration of Queen Mary University of London with the support of PwC found that:

While, overall, arbitration remains the preferred dispute resolution mechanism for transnational disputes, many respondents and interviewees expressed concern over the related issues of costs and delays experienced in international arbitration proceedings.<sup>41</sup>

The bigger the amount in dispute, the higher the chances that several objections would be raised during the course of the arbitration proceedings. When parties raise objections or make requests during arbitral proceedings, additional costs would be incurred. This is because it might be necessary for a party to file a motion/application to which the other party would have to react by filing a response in the interest of fair hearing. In regard to this issue, Berger & Jensen observed that:

Such requests place international arbitrators in a true dilemma. On one hand, they must ensure the time and cost efficient conduct of the proceedings. On the other, such requests touch upon the core of the parties' due process rights. Will ignoring an unsolicited submission cause the party to argue a violation of its right to be heard? Does the dismissal of a new claim late in the arbitration infringe upon the party's right to present its case?<sup>42</sup>

By virtue of Article V 1 (d) of the New York Convention,<sup>43</sup> Recognition and enforcement of an award may be refused at the request of the party against whom it is invoked if the arbitral procedure was not in accordance with the agreement of the parties, or failing such agreement, was not in accordance with the law of the country where the arbitration took place.

The above provision recognises two sources of arbitral procedure: one being by agreement of parties and the other being in accordance with the law of seat of arbitration. Parties to an arbitration

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41 Queen Mary University of London, '2013 International Arbitration Survey – Corporate choices in International Arbitration: Industry Perspectives' (2013) <<http://www.arbitration.qmul.ac.uk/media/arbitration/docs/pwc-international-arbitration-study2013.pdf>> accessed 24 February 2019.

42 Klaus Peter Berger and J. Ole Jensen, 'Due process paranoia and the procedural judgment rule: a safe harbor for procedural management decisions by international arbitrators', in João Bosco Lee and Daniel de Andrade Levy (eds), *Revista Brasileira de Arbitragem*, (© Comitê Brasileiro de Arbitragem CBAr & IOB; Kluwer Law International 2017, Volume XIV Issue 54) pp. 73 – 94, 77.

43 New York Convention (n 34).

agreement usually have the autonomy to agree on the arbitral procedure subject to minimal mandatory restrictions of national legislations.<sup>44</sup> However, “parties in practice often do not agree in advance on detailed procedural rules. Instead, arbitration agreements ordinarily provide simply for arbitration pursuant to a set of institutional rules, which supply only a broad procedural framework.”<sup>45</sup>

During arbitral proceedings, parties may subsequently determine the procedure to be adopted on specific issues which were not initially agreed upon or specifically covered by the broad procedural framework. Where parties fail to agree on an arbitral procedure, the arbitral tribunal usually have discretion to determine the appropriate procedure. Section 41(3) of the Arbitration Act<sup>46</sup> gives the tribunal discretionary power to dismiss a claim if it is satisfied that there has been inordinate and inexcusable delay on the part of the claimant which:

- (a) gives rise, or is likely to give rise, to a substantial risk that it is not possible to have a fair resolution of the issues in that claim, or
- (b) has caused, or is likely to cause, serious prejudice to the respondent, the tribunal may make an award dismissing the claim.<sup>47</sup>

The first problem with the above provisions is that first, it is not mandatory and parties can agree otherwise. Secondly, the power to dismiss could only be exercised in favour of a respondent whereas a respondent could equally engage in similar conducts which could prejudice the interests of a claimant as was the case in *Trunk Flooring*<sup>48</sup> where a respondent refused to pay for the advance cost of arbitration of the ICC after having made a counterclaim which significantly increased the arbitration fee. Other than the provisions of section 41 (3), section 41, in absence of parties agreement to the contrary, gives the tribunal other discretionary powers to ensure fair resolution of a case. Such powers however are not easy to exercise because of ‘due process paranoia’.

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44 Gary B. Born, *International Arbitration: Law and Practice* (2<sup>nd</sup> edn, Kluwer 2015).

45 *ibid.*

46 Arbitration Act 1996.

47 *ibid*

48 [2015] NICA 68.



Even though the arbitral tribunal usually enjoys broad discretion to determine the appropriate procedure in arbitral proceedings, which is one of the defining features of arbitration, ‘[i]t is subject to an overarching respect of due process or natural justice—that is, equality of treatment and an opportunity to be heard.’<sup>49</sup> In regard to tribunal’s discretion, klaus & Jensen argued that:

[A]rbitral discretion and the powers it entails appear more like a toothless tiger than a key tool for the efficient conduct of the proceedings. Indeed, such a generic and overzealous understanding increases the arbitrators' reluctance to conduct the arbitration proactively and endangers streamlined proceedings. After all, dealing with additional submissions, extending deadlines or postponing hearings affects all three: time, costs and the quality of the arbitration.<sup>50</sup>

What constitutes “equality of treatment” depends on the “circumstances of the parties’ respective positions, claims and evidence, and the arbitral process as a whole.”<sup>51</sup> In regard to equality of treatment, Born observed that “The concept of equality of treatment is essentially a requirement of non-discrimination. All parties to the arbitration must be subject to the same procedural rules and afforded the same procedural rights and opportunities.”<sup>52</sup> He observed further that:

Application of the principle of equal treatment also requires careful consideration of the context in which the treatment occurs. In practice, it is almost impossible to treat parties perfectly equally or identically, either in terms of time and other opportunities allowed for presenting their case. Inevitably, the differences between the parties’ positions will make identical treatment both impossible and, in many cases, unimportant.

For example, it is impossible to grant both the claimant and respondent identical amounts of time to prepare their cases. This is because the claimant has “as long as it likes within statutory limitation periods to prepare and bring the claim,” but the respondent will normally have a much shorter period of time to prepare an answer. Moreover ... exact equality of time (*e.g.*, both parties are permitted 12 ½ hours to present their cases) may, in some

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49 Nigel Blackaby and others, *Redfern and Hunter on International Arbitration* (6<sup>th</sup> edn, OUP 2015) 308.

50 Berger & Jensen (n 42) 78.

51 Blackaby and others (n 49).

52 Gary B. Born, *International Commercial Arbitration*, (2<sup>nd</sup> edn, Kluwer 2014) 2173.

circumstances, not amount to equal treatment and may, instead, be unequal and unfair – because one party’s case may, by its nature, take longer to present.<sup>53</sup>

Although denial of ‘equality of treatment’ may constitute denial of ‘opportunity to be heard’ in some cases, this is not always the case. ‘Equality of treatment’ is different because it means in effect affording a party what was afforded to another party. Refusal to grant a party an equal time granted to the opposition party in leading evidence for example might constitute denial of equal treatment. Whereas not determining an issue raised by a party in the proceedings, such as a claim, on the other hand might constitute denial of an opportunity to be heard.

In order to avoid breaching the requirement of due process, arbitrators are likely to adjourn proceedings several times at the request of parties. The problem with conformity with fair hearing is that while there may be legitimate requests for adjournment, some parties usually abuse it in order to delay or frustrate proceedings. In what seems to be an attempt to tackle the problem of abuse of due process requirements, the LCIA made a 7 paragraph annexe to its arbitration rules. The annexe contains guidelines, purpose of which, was to promote good and equal conduct of parties’ legal representatives appearing by name within the arbitration. Paragraph one of the annexe states that:

... Nothing in these guidelines is intended to derogate from the Arbitration Agreement or to undermine any legal representative’s primary duty of loyalty to the party represented in the arbitration or the obligation to present that party’s case effectively to the Arbitral Tribunal. Nor shall these guidelines derogate from any mandatory laws, rules of law, professional rules or codes of conduct if and to the extent that any are shown to apply to a legal representative appearing in the arbitration.<sup>54</sup>

Paragraph 2 of the annexe provides as follows:

A legal representative should not engage in activities intended unfairly to obstruct the arbitration or to jeopardise the finality of any award, including repeated challenges to an arbitrator’s appointment or to the jurisdiction or authority of the Arbitral Tribunal known to be unfounded by that legal representative.

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<sup>53</sup> *ibid* (citations omitted).

<sup>54</sup> London Court of International Arbitration ‘Arbitration Rules’ (2014)

<[http://www.lcia.org/Dispute\\_Resolution\\_Services/lcia-arbitration-rules-2014.aspx](http://www.lcia.org/Dispute_Resolution_Services/lcia-arbitration-rules-2014.aspx)> accessed 1 May 2017

The problem with the guidelines is that where an arbitral award is challenged, it could be a defence to the challenge that an objection was not raised during the arbitration proceedings. In this regard section 73 (1) of the Arbitration Act provides that:

If a party to arbitral proceedings takes part, or continues to take part, in the proceedings without making, either forthwith or within such time as is allowed by the arbitration agreement or the tribunal or by any provision of this Part, any objection-

1. (a) that the tribunal lacks substantive jurisdiction,
2. (b) that the proceedings have been improperly conducted,
3. (c) that there has been a failure to comply with the arbitration agreement or with any provision of this Part, or
4. (d) that there has been any other irregularity affecting the tribunal or the proceedings, he may not raise that objection later, before the tribunal or the court, unless he shows that, at the time he took part or continued to take part in the proceedings, he did not know and could not with reasonable diligence have discovered the grounds for the objection.<sup>55</sup>

In other words, failure to raise such objection would constitute a waiver. Legal representatives thus, could be said to have a duty, according to rules of law, to raise objections where necessary. Thus to avoid being estopped from challenging an award at a later stage, legal representatives tend to raise several objections during arbitral proceedings. Both claimant's and respondent's counsel are likely to raise the objections so as to have something to rely on should in case the arbitral award is not in their favour.

The tribunal's duty to prevent delay, for instance, is not always an easy task such as in proceedings where an amendment is made to the pleadings of one party. Parties may need to amend their pleadings at some point because of a mistake or to include newly arising facts which are pertinent to their claim or defence. Arbitrators thus, usually permit a party to make an amendment. The provision for amendment is contained in many institutional rules and Arbitration Laws. In some cases, an amendment could be made to the Notice of Arbitration itself which could have an effect

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<sup>55</sup> LCIA Arbitration Rules (n 13).

on the procedural timeframe and costs. Pursuant to Article 18 of the HKIAC Rules<sup>56</sup>, for instance, an amendment could lead to adjustment of the cost of the administrative fees and tribunal fees. If more claims are added to the statement of claim, this could consequently increase the cost of the arbitration.

In regard to applications for amendment, arbitrators in essence usually have two important duties which they have to exercise with discretion: one is affording parties the opportunity of being heard and the other is ensuring that proceedings are concluded timely without unnecessary delay. They need to exercise their discretion with a balance between these two requirements because a breach of any of these duties may lead to an award being set aside in some cases.

Although parties may represent themselves in arbitration, they may also choose to be represented by a legal representative and that is usually the case. Where parties are represented by legal representative, a party may need to change its legal representative and arbitrators usually have discretion to adjourn the proceedings to afford the party time to instruct new legal representative. The new legal representative may subsequently seek an adjournment in order to have time to familiarize himself with the facts of the case. In some cases, the arbitrator may refuse to grant an application for change of legal representative if he thinks that the change would cause unnecessary delay or costs in the proceedings. In deciding whether or not to allow grant a party an adjournment in such cases, the tribunal would need to balance the right of opportunity to heard on one hand and the need to conduct the proceedings without unnecessary delay.

One party's amendment would also necessitate that the other party amend its own pleading as well. Such amendments would involve an increase in the cost of legal representatives and it is not unusual for a legal representative to seek to withdraw service due to unpaid fees at a late stage in the proceedings. Consequently, the client may need to change legal representative if he/she could afford the service of another legal representative who would charge less or he/she may have to negotiate for settlement on favourable terms to the other party. If the party decides to change counsel, the decision would still lie to the arbitrator who may refuse the application for change of

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56 Hong Kong International Arbitration Centre, 'Administered Arbitration Rules' (2018)

<[http://www.hkiac.org/sites/default/files/ck\\_filebrowser/PDF/arbitration/2018\\_hkiac\\_rules.pdf](http://www.hkiac.org/sites/default/files/ck_filebrowser/PDF/arbitration/2018_hkiac_rules.pdf)> accessed 24 February 2018; Stockholm Chamber of Commerce 'Arbitration Rules' (2017)

legal representative in the spirit of preventing further delays and costs in the proceedings. By such decision, the opposing party will have achieved its aim of frustrating the other party's claim.

It is not unusual for an economically superior party to call an expert witness, whose service would be expensive, thus necessitating that the other party calls an expert witness as well to refute an evidence led by the other party's witness. This could tactically create additional expenses for the economically inferior party and prejudice their chances of achieving a fair resolution of the trial.

Furthermore, unless parties have agreed to a document-only arbitration, parties may need to secure the attendance of a witness for oral hearing. Attendance of a witness may be difficult to procure at times. This may be due to other commitments which the witness has such as work or family life. In view of this, a party may need to seek an adjournment of the arbitral proceeding to secure the attendance of the witness at a later time and the tribunal might adjourn to afford the party an opportunity of being heard.

## **2.4 Financial stamina of the economically inferior party**

Increased costs in arbitral proceedings could consequently frustrate economically inferior parties out of the proceedings. By economically inferior, I meant the party with less financial stamina or in other words, an impecunious party. I used the term 'economically inferior' at the onset because impecuniosity connotes two meanings, to wit having little or no money. A party with no money would not have reasonably agreed to settle dispute by arbitration in the first place if at least such party were aware that arbitration involves some costs.

The term 'economically inferior' on the other hand implies that the party in question has a lower financial status compared to that of the counterparty. To better understand this, one could use a boxing match as an analogy. In a boxing match of 12 rounds, a contender might have the strength to land devastating punches but without stamina he might not be able to fight till the end. If his opponent is aware of such weakness, he is very likely to use it to his own advantage by ensuring that the contest lasts the whole 12 rounds. The hypothetical strength to land devastating punches could be compared to the strength of a party's case in arbitration while the stamina could be compared to his financial ability to pursue his claim (in other words, financial stamina). Without

financial stamina to pursue the claim to the end, the party is unlikely to succeed in the proceedings. The Californian Court of Appeal right observed in *Weiler* that:

[F]rom a public policy standpoint, a defendant accused of wrongdoing should not be permitted to avoid potential liability by forcing the matter to arbitration and subsequently making it so expensive that the plaintiff eventually has no choice but to give up. To hold otherwise would be to turn ““and justice for all”” into ““and justice for those who can afford it”” and ““threaten the very underpinnings of our social contract.”” (*Alan S. v. Superior Court* (2009) 172 Cal.App.4th 238, 263, fn. 25.) The interest in avoiding such an outcome far outweighs the interest, however strong, in respecting parties’ agreements to arbitrate.<sup>57</sup>

Legal representatives are more likely to engage in activities that might constitute abuse of procedural due process if they feel that their client might not have a strong case or because they do not want to be estopped from raising such issues in the court at a proceeding for review of the award, in the event that they are unsatisfied with the award or any part of it. These activities, which delay and increase the costs of proceedings, could be contagious because a lawyer representing the other party is likely to engage in such activities as well. This might be because he does not want to appear as incompetent to his client or because he does not want to be likewise estopped from raising objections at a later stage. Not surprisingly, the SIA 2013 survey found that:

A recurrent theme in interviews with respondents from various sectors was the risk of “judicialisation” of arbitration. Interviewees expressed concern about their perception that the process of arbitration has become more sophisticated and more “regulated”, with “control” over the process moving towards law firms – and away from the actual users of this process.<sup>58</sup>

While it could be a common assumption that wealthy parties have a tendency to fulfil all their financial obligations, this is not always the case. I recall Donald Trump being accused by Hilary Clinton during the US presidential election campaign debate in 2016 that he did not fulfil all his tax

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<sup>57</sup> 2018 WL 2011048 (Cal. Ct. App. 4th Dist. no. G053953 (Apr. 30, 2018)).

<sup>58</sup> Queen Mary University of London, ‘2013 International Arbitration Survey: Corporate choices in International Arbitration: Industry Perspectives’ (2013) <<http://www.arbitration.qmul.ac.uk/media/arbitration/docs/pwc-international-arbitration-study2013.pdf>> accessed 24 February 2019.

obligations. His response was that he used the tax law to his advantage. He was also quoted as saying 'he has had a "fiduciary responsibility" to "pay as little tax as legally possible."' <sup>59</sup> The statement of Holmes in regard to how businessmen approach the law could not be truer. He stated thus:

The first thing for a businesslike understanding of the matter is to understand its limits, and therefore I think it desirable at once to point out and dispel a confusion between morality and law, which sometimes rises to the height of conscious theory, and more often and indeed constantly is making trouble in detail without reaching the point of consciousness. You can see very plainly that a bad man has as much reason as a good one for wishing to avoid an encounter with the public force, and therefore you can see the practical importance of the distinction between morality and law. A man who cares nothing for an ethical rule which is believed and practised by his neighbors is likely nevertheless to care a good deal to avoid being made to pay money, and will want to keep out of jail if he can <sup>60</sup>.

He stated further that:

If you want to know the law and nothing else, you must look at it as a bad man, who cares only for the material consequences which such knowledge enables him to predict, not as a good one, who finds his reasons for conduct, whether inside the law or outside of it, in the vaguer sanctions of conscience. <sup>61</sup>

If one applies Holmes' theory to how economically superior parties deal with arbitral proceedings, it means in essence that a wealthy party could try to do everything possible in the confines of the law to avoid an award which would not be in his favour or to frustrate a claim against him if possible. Going back to the hypothetical boxer who would run around the ring with the hope of exhausting his much stronger opponent. His tactic could earn him a victory at the end, even though

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59 Sean Sullivan, Washington Post 3 October 2016

<[https://www.washingtonpost.com/news/post-politics/wp/2016/10/03/trump-says-he-brilliantly-used-tax-laws-to-his-advantage/?noredirect=on&utm\\_term=.1e68a281e577](https://www.washingtonpost.com/news/post-politics/wp/2016/10/03/trump-says-he-brilliantly-used-tax-laws-to-his-advantage/?noredirect=on&utm_term=.1e68a281e577)> accessed 23 March 2019.

60 Oliver W. Holmes, *The Path of the Law*, 10 Harvard Law Review 457 (1897).

61 *ibid*

spectators from the audience might think he is not a good fighter. In the end however, all that matters is victory.

In light of the foregoing analysis, one can thus conclude that activities centered around conformity with the requirements of procedural due process can affect the financial ability of an economically inferior party to prosecute its case in an arbitration proceeding. This leaves a question of what options are available to such party in the prosecution of its case. This issue shall be examined in the next chapter.

### **3 Courts' approach to the issue of impecuniosity of a party as an impediment to the attainment of justice**

#### **3.1 The approach in UK**

In the case of *Janos Paczy v Haendler & Natermann Gmbh*<sup>62</sup>, the English Court of Appeal had to decide a matter concerning the right of an impecunious party to seek remedy in court due to his inability to commence arbitral proceedings. The parties in the case were Janos Paczy (plaintiff) and Haendler & Natermann Gmbh (defendant), a German company.

By a contract dated 23rd October, 1974, the plaintiff granted licence to defendant, to manufacture and sell airgun pellets in accordance with a method of manufacture which the plaintiff claimed to have invented. Pursuant to the agreement, defendant was to pay royalties on the sales of the product. Clause 12 of the contract stipulated that:

Any dispute arising out of or in connection with this Agreement shall be settled with recourse to the Courts in accordance with the Rules of Conciliation and Arbitration of the

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<sup>62</sup> 1981 WL 188128.



International Chamber of Commerce. The arbitrators shall have power to rule on their own competence and on the validity of the Agreement to submit to Arbitration.<sup>63</sup>

On the 12th October, 1978 the plaintiff commenced an action against the defendant in the High Court alleging that the defendant had breached the contract by failing to submit royalty accounts and failing to pay royalties in accordance with the contract. The plaintiff further alleged that he terminated the agreement on 10th July, 1978, and that since then, the defendant had wrongfully made use of confidential information which they had obtained under the agreement. In that action, the plaintiff obtained a legal aid certificate for the purpose of prosecuting the action ‘with a nil contribution’.

Subsequently, the defendant applied for stay of proceedings pursuant to section 1, subsection 1 of the Arbitration Act 1975, provisions of which is similar to that of section 9 of the Arbitration Act 1996. The said provision of subsection 1 gives effect to the provision of article II, paragraph 3 of the New York Convention by imposing a mandatory duty on the court to stay proceedings unless it finds that the agreement to arbitrate null and void, inoperative or incapable of being performed. Section 1(1), provides that:

If any party to an arbitration agreement to which this section applies, or any person claiming through or under him, commences any legal proceedings in any court against any other party to the agreement, or any person claiming through or under him, in respect of any matter agreed to be referred, any party to the proceedings may at any time after appearance, and before delivering any pleadings or taking any other steps in the proceedings, apply to the court to stay the proceedings; and the court, unless satisfied that the arbitration agreement is null and void, inoperative or incapable of being performed or that there is not in fact any dispute between the parties with regard to the matter agreed to be referred, shall make an order staying the proceedings.<sup>64</sup>

An affidavit was filed in support of the summons, stating that the matters in dispute were matters within the scope of the arbitration agreement and that the defendants ‘were ready and willing to do

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<sup>63</sup> *ibid.*

<sup>64</sup> Arbitration Act 1975.

and concur in all things necessary for causing the dispute to be decided by arbitration'.<sup>65</sup> Evidence was filed in answer in an affidavit of one Mr. Fordham stating that the plaintiff was a legally aided person and that if the action were stayed, he would have difficulty in meeting the costs of arbitration proceedings because legal aid was not available for such proceedings. The plaintiff himself also deposed to an affidavit wherein he stated that he was unemployed and relied on unemployment pay and on social security benefit. He stated that he would not be unable to finance arbitration proceedings.

In regard to the costs of the arbitration. Article 9 of the relevant ICC rules provided:

1. The court shall fix the amount of the deposit in a sum likely to cover the costs of arbitration of the claims which have been referred to it.
2. As a general rule, the deposits shall be paid in equal shares by the Claimant or Claimants and the Defendant or Defendants. However, any one party shall be free to pay the whole deposit in respect of the claim or the counterclaim should the other party fail to pay a share.<sup>66</sup>

The application for stay was granted by the high court. Thereafter, the plaintiff did not commence arbitration proceeding due to his alleged impecuniosity. The defendant likewise did not commence any arbitration proceeding. Subsequently, the plaintiff, through his solicitor enquired of the defendant as to when they will commence arbitration proceedings and defendant's solicitor, referring to the provisions of the ICC rules, replied that the defendant has no obligation to commence the arbitration proceeding and that the burden of commencement of the arbitration is on the plaintiff. For sake of emphasis, the following correspondence ensued between the parties:

In May, 1979 the plaintiff's solicitors wrote to defendant's solicitors saying:

You will be aware that our client is not in a financial position to proceed to arbitration, and in view of the Judge's order that if the matter is not referred to arbitration promptly either party may again apply to the court, we would be grateful if you would inform us as soon as

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<sup>65</sup> *Paczy* n 62.

<sup>66</sup> *Paczy* n 62.

your clients have referred the matter to arbitration under the rules of the International Chamber of Commerce. We look forward to hearing that this has been done within the next few weeks.<sup>67</sup>

Defendant's solicitors replied that 'If our clients choose not to refer the matter to arbitration, we can see no grounds upon which your client could then apply to the court for his proceedings to be reinstated.'<sup>68</sup> Correspondence continued between the parties and on 28th June, the defendant's solicitors wrote:

You appear to suggest that there is some burden on our clients to commence the arbitration. Reference to the ICC rules shows (as one would expect) that it is the claimant who must initiate matters. In particular, under Article 3 the claimant must make the request for arbitration and put in his statement of case. If and when your client does this, our client will respond under the ICC rules.<sup>69</sup>

Eventually, the matter came up again before the high court on 9th July 1979 and the learned judge in removing the stay held as follows:

Where you have an agreement that any dispute arising in connection with an agreement shall be settled and it is claimed that there is a dispute – the Plaintiff contends that he is owed money and the Defendants contend that he is wrong – and you get a situation in which the one party (the Plaintiff) wants the matter settled and the other party (the Defendants) say it should be settled but only by arbitration, and the situation in practical terms is that the Plaintiff cannot bring the arbitration and the Defendant will not, then it is, as a matter of common sense, an arbitration agreement that is incapable of being performed.<sup>70</sup>

The court of appeal was faced with the determination of the following issue:

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<sup>67</sup> *ibid.*

<sup>68</sup> *ibid.*

<sup>69</sup> *ibid.*

<sup>70</sup> *ibid.*

1. The proper construction and effect of section 1(1),<sup>71</sup> particularly the phrase “incapable of being performed”.

Plaintiff’s counsel argued that:

[T]he court should construe Section 1 of the Act of 1975 in a broad way so as to give it a sensible common sense practical effect, and that the words “incapable of being performed” should be construed in the sort of way in which I think Mr. Justice Whitford was indeed prepared to read them, so that any case in which there was a real practical difficulty in proceeding with the arbitration proceedings would be one which could be described as having become incapable of performance within the meaning of the section.

It is worth noting that the plaintiff’s counsel’s argument envisages not only a situation in which a party has difficulty in commencing arbitration proceedings but also situations where a party could have ‘real practical difficulty in proceeding with the arbitration proceedings’. This line of reasoning, as will be later seen, resonates with the reasoning in the approach of US courts in similar matters involving the impecuniosity of a parties.

In considering the question of whether the arbitration agreement had become incapable of being performed, the Court of Appeal, per Buckley, LJ, held that:

I am prepared to assume in the Plaintiff’s favour that he is incapable of finding the deposit, although I am bound to say that I am not at all satisfied that the evidence establishes that in at all an absolute sense. In my judgment, on the true construction of these words, “incapable of being performed” relates to the arbitration agreement under consideration. The incapacity of one party to that agreement to implement his obligations under the agreement does not, in my judgment, render the agreement one which is incapable of performance within the section any more than the inability of a purchaser under a contract for purchase of land to

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<sup>71</sup> *ibid.*

find the purchase price when the time comes to complete the sale could be said to render the contract for sale incapable of performance. The agreement only becomes incapable of performance in my view if the circumstances are such that it could no longer be performed, even if both parties were ready, able and willing to perform it. Impecuniosity is not, I think, a circumstance of that kind.<sup>72</sup>

In so holding, the learned justice seems to overlook the fact that the plaintiff was actually willing to participate in an arbitration proceeding as evidenced by the letters which his solicitors wrote to the defendant but was unable to commence the proceeding due to impecuniosity. Rather, the learned justice seems to place a very narrow interpretation on ‘incapable of being performed’.

The learned judge of the high court emphasised in his ruling that ‘the situation in practical terms is that the Plaintiff cannot bring the arbitration and the Defendant will not, then it is, as a matter of common sense, an arbitration agreement that is incapable of being performed’.<sup>73</sup> The fact that the learned trial judge stayed the proceedings and made an order that ‘the parties are to be at liberty to apply’<sup>74</sup> implies that he had anticipated that, during the time when the proceeding was stayed, the parties would resolve between themselves how the matter was to be prosecuted vide arbitration proceedings.

The defendant’s unwillingness to commence arbitration proceedings or provide the advance costs of the arbitration proceedings after obtaining an order of stay seems to be a new circumstance which occurred after the order for stay was granted. These circumstances seem to be overlooked by the learned justice of the court of appeal when he held that:

... the court is under an obligation to stay the proceedings at law unless the agreement is null and void, inoperative, or incapable of being performed. If it could be shown that, owing to events which occurred since the stay was imposed, the arbitration agreement had become incapable of performance I think the court would very probably be right in lifting the stay. But it seems to me that, unless the circumstances at the time when the matter was before the learned Judge in July last were such that if a stay had then been sought it could properly

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<sup>72</sup> *ibid.*

<sup>73</sup> *ibid*

<sup>74</sup> *ibid*

have been refused, it cannot have been right for the learned Judge to lift the stay which he had earlier granted. In the circumstances of the present case it seems to me that if a stay had been sought in July, 1980 the circumstances were not then such, and I do not think they are such today, as would have made it proper to refuse the stay.

The English court again, per Tomlinson J, in *Amr Amin Hamza EL Nasharty v J. Sainsbury Plc*<sup>75</sup> reiterated the decision in *Paczy* by stating that:

... inability of one party to meet his financial obligations under the ICC or comparable Rules or procedures does not render the arbitration agreement inoperative or incapable of being performed — see *Janos Paczy v Haendler and Natermann [1981] 1 Lloyds Rep 302*, concerned with the materially identical section 1 of the Arbitration Act 1975. Brightman LJ in that case indicated that in his view it cannot have been intended by Parliament that the court should on an application such as this attempt to assess the financial resources of a party.<sup>76</sup>

Nevertheless, Tomlinson J, went on to comment on the evidence adduced by the claimant in *Nasharty* in support of his alleged impecuniosity and stated that ‘the evidence as a whole falls far short of satisfying me that the Claimant does not have access to resources which would enable him to pursue his claims against Sainsbury in his chosen forum, arbitration’<sup>77</sup>. Perhaps the learned judge would have come to a different conclusion, had the claimant adduced sufficient credible evidence to support his alleged impecuniosity. Still, it is difficult for the court to reach a different conclusion from that in *Paczy*, decision of which is binding being a decision of a superior court. Such attempt might require the court to distinguish the facts of both cases.

In *BDMS Limited v Rafael Advanced Defence Systems*<sup>78</sup>, The claimant was a limited company incorporated in England while the defendant was a limited company incorporated in Israel and

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<sup>75</sup> [2007] EWHC 2618 (Comm)

<sup>76</sup> *ibid.*

<sup>77</sup> *ibid.*

<sup>78</sup> [2014] EWHC 451 (Comm)

wholly owned by the government of Israel. The dispute between the parties concerned sums allegedly due to the Claimant from the Defendant by way of 'success fees' under a consultancy agreement, which was executed by representatives of the defendant. Clause 7 of the Agreement provided that dispute between the parties shall be resolved by arbitration under the rules of ICC and that London shall be the seat of arbitration. Article 30 (3) of the said ICC rules provided that:

The advance on costs fixed by the Court shall be payable in equal shares by the Claimant and the Respondent. Any provisional advance paid on the basis of Article 30(1) will be considered as a partial payment thereof. However, any party shall be free to pay the whole of the advance on costs in respect of the principal claim or the counterclaim should the other fail to pay its share.<sup>79</sup>

In April 2011, the claimant filed a request for arbitration with the ICC in regard to its claim against the defendant and the defendant filed its Answer to the request for arbitration in June 2011. In October 2011, a sole arbitrator was appointed by the ICC, in accordance with the arbitration agreement. On 3 November 2011 the ICC wrote the parties in respect of advance on costs which was fixed 27,000 USD and invited the Claimant to pay US\$1,500 USD being the balance of its share of the advance on costs having given credit for payment of provisional advance, and the Defendant was required to pay 13,500 USD.

The Defendant's solicitors had expressed concerns about the claimant's ability in meeting any adverse costs order and on 7 November 2011 they wrote to the Claimant's legal representative stating that:

“[A]s you will have seen from our letter to the arbitrator of 2 November 2011, our client intends to make an application that BDMS be ordered to provide security for Rafael's costs. In light of the ICC's request that Rafael contribute USD\$13,500 to the advance on costs, we write to put you on notice that, until adequate security has been put in place, Rafael does not propose to pay the advance on costs.”<sup>80</sup>

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<sup>79</sup> *BDMS* (n 78), para 7.

<sup>80</sup> *ibid*, para 11.

On 1 December 2011 the tribunal held a meeting with the parties where terms of reference were agreed by both parties. The terms provided, *inter alia*, that one of the issues to be determined in the arbitration is “payment of the advance on costs.” On 21 December 2011, the tribunal made procedural directions providing for a preliminary hearing on 19 March 2012. Under paragraph 7 of the directions, one of the matters to be dealt with was “any issues relating to the non-payment to the ICC of an advance on costs.”

In a letter of 28 December 2011 written to the parties, ICC acknowledged the claimant's payment of its outstanding share of the advance on costs and demanded again that the defendant should pay its share of the advance on costs within 15 days from receipt of the letter. On 17 January 2012 ‘the defendant made an application to the tribunal for an order of security for costs against the claimant, requesting that the application be heard at the hearing on 19 March 2012.’

On 18 January 2012, ICC wrote to the parties in regard to the defendant's failure to pay its share of the advance on costs and invited the claimant to substitute for the defendant in paying its share of the advance by 1 February 2013. After further correspondence and following non-receipt of the balance of the advance of costs after repeated demands, the ICC consequently withdrew the claimant's claim.

The claimant subsequently decided to treat defendant's failure to pay his share of the advance on costs as a repudiatory breach of the arbitration agreement and went back to court to pursue its claim. The defendant contended that there was no repudiatory breach and opposed the lifting of the previously granted stay of proceedings. He contended that the arbitration agreement has not become inoperative.

Among the issues highlighted by the court for determination were the following:

(1) Whether there was a breach of the arbitration agreement.

(2) Whether the arbitration agreement was “inoperative”.<sup>81</sup>

### **Whether there was a breach of the arbitration agreement**

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81 *BDMS* (n 78) para 39



The court noted, in reference to ICC arbitration decisions and commentaries thereon, that there are two different views on this issue, to wit ‘whether the requirement that an advance on costs be paid under Article 30(3) gives rise to a contractual obligation (contractual approach) owed to the other party or merely to a procedural obligation (interim measure approach) owed to the ICC Court.’ The court stated that the former view could give rise to a substantive claim and an interim award may be rendered. In regard to the latter view, court stated that the issue is one of procedure rather than substance and an arbitrator in such case could grant interim measures.

On the contractual approach, the court, citing a view expressed in ASA Bulletin<sup>82</sup> stated that:

According to contractual approach, both the legal basis of the claim and the arbitral tribunal's competence are based on two elements: (i) that Article 30(3) ICC Rules (or a similar provision in other arbitral rules) gives rise to reciprocal contractual obligation between the parties to pay the advance of costs because this contractual term was made part of the arbitration agreement by reference to the relevant rules; and (ii) that a dispute with respect to this obligation falls within the scope of the arbitration agreement between the parties. The contractual approach has been followed by what seems to be the majority of arbitral and court decisions on the subject and has been endorsed by most authors. The proponents of this approach consider the non-payment of the advance on costs a breach of a contractual obligation giving rise to a substantive claim. ...<sup>83</sup>

On the interim measure approach, the court stated that advocates of the approach emphasise that any decision of an arbitral tribunal ordering a party to pay an advance on costs is a procedural decision of administrative nature and thus not subject to review by state courts.<sup>84</sup>

In determination of the issue the court stated that the majority of arbitral and court decisions favour the contractual approach, as do the majority of commentators. That as a matter of English law, the approach is consistent with the contractual agreement to arbitrate under the Rules of the ICC and the mandatory terms in requiring payment of advance on costs. The court emphasised that the

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82 M. Buhler, ASA Bulletin 2/2006 at p290–301.

83 *BDMS* (n 78) para 42.

84 *BDMS* (n 78).

contractual approach is also consistent with the only common law court decision to which it was referred, namely the decision of the Alberta Court of Appeal in *Resin Systems Inc. v Industrial Service & Machine Inc.*,<sup>85</sup> which emphasised the breach of a mandatory rule by the “defaulting party”.

The court thus concluded that failure to pay the advance required under Article 30(3) of the ICC Rules does involve a breach of the arbitration agreement. It was stated further that, regardless of the correct approach, it is well established that the tribunal can order a defaulting party to pay the advance on costs, either by rendering an interim award or by making an interim measure.

### **Whether the arbitration agreement was inoperative**

Having determined that there was no breach of the arbitration agreement, the court then went on to consider whether the breach was repudiatory. In my opinion, this was an unnecessary exercise on the part of the court since it was held that there was no breach in the first place. However, while considering the issue of whether there was a repudiatory breach, the court gave reasons which it later stated were equally applicable in deciding whether the arbitration agreement was inoperative.<sup>86</sup> Thus, in holding that the arbitration agreement has not become inoperative, the following reasons were stated by the court:

- i. The case is not one in which the Defendant was refusing to participate in the arbitration. It was actively participating in the arbitration but would not pay for his share of the advance on costs unless security for costs was provided by the claimant.
- ii. That breach did not deprive the claimant of its right to arbitrate. ‘It was at all times open to the Claimant to proceed with the arbitration by posting a bank guarantee for the Defendant’s share and then seeking an interim award or interim measure order that the advance be paid by the Defendant.’ In any view, the claimant could have sought such an order in a final award. It could also have objected against withdrawal to the ICC Court pursuant to Rule 30(4).

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<sup>85</sup> [2008] ABCA 104.

<sup>86</sup> *BDMS* (n 78) para 59.

iii. Even though it is correct to say that the claimant did not have an obligation either to pay the defendant's share of advance costs or to object to withdrawal of the claim, the Rules provide means of proceeding with the arbitration and avoiding withdrawal of the claim.

iv. By virtue of the Rules of the ICC, the withdrawal of the claim due to default in payment of the advance on costs does not prevent the same claim being brought to arbitration again at a future time.

The problem with the above reasoning is that the court, in suggesting the the claimant could have posted a bank guarantee to cover the defendant's share of the advance costs, seems to overlook the fact that the financial ability of the claimant was a concern raised by the defendant in demanding security for costs. There was thus, an inference that the claimant was an economically inferior party and nevertheless endeavoured to fulfil its own obligation on the advance costs by paying its share. The defendant on the other hand, by insisting on the hearing of his application on security for costs before payment of his share of the advance costs, stultified the proceedings which later led to the withdrawal of the claim by the ICC.

The scenario caused by the defendant in the case creates a difficult situation for an economically inferior party. Let us assume that the claimant asserts that he could not afford to pay for the defendant's share of the advance on costs. This would, in effect, justify the defendant's assertion on its concern for the claimant's financial capacity and further fortify its stance on refusal to pay the advance on costs. On the other hand if the claimant could not afford to pay for the defendant's share without an assertion of its financial ability, the deadlock still remains.

In *Trunk Flooring Limited v HSBC Asset Finance (UK) Limited, Costi Righi SPA*,<sup>87</sup> the appellant was a manufacturer of plant and machinery used for processing of timber flooring. In 2008 the respondent entered into a hire purchase agreement with the first defendant in respect of a machine manufactured by the appellant and paid a deposit of £73,000 with remaining balance of the purchase price to be obtained by credit. The machine was then purchased by the respondent.

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87 [2015] NICA 68

Dispute arose between the appellant and the respondent because the machine allegedly failed to operate properly and the respondent claimed to have sustained loss due to the appellant's alleged negligence and breach of contract. The respondent's claim include £193,000 being the cost of purchase, increased costs amounting to £21,000, £700,000 being loss of profits in the North American market and an additional loss of profits of £325,000 with the total amount of the claim adding up to £1.249m.

The contract between the parties contained an arbitration clause which provided that any dispute arising out of the contract should be settled under the Rules of Conciliation and Arbitration of the International Chamber of Commerce by arbitrators appointed in accordance with the Rules. Subsequent to the respondent commencing proceedings in court for breach of contract and negligence, the appellant applied for a stay of the proceedings under section 9 of the Arbitration Act 1996 so that the dispute might be resolved by arbitration. The court stayed the proceedings pending arbitration and ordered that unless the arbitration proceedings commence within 28 days from the date of the order, the stay against the second named defendant shall be lifted.

The appellant subsequently submitted a request for arbitration and various steps were taken over some 18 months that followed. Eventually an impasse, for which the parties blamed each other, emerged between the parties over the question of costs.

Article 36 of the relevant ICC arbitration rules provided that:

[A]fter receipt of the request the Secretary General may request the claimant to pay a provision in advance in an amount intended to cover the costs of the arbitration until the terms of reference have been drawn up. As soon as practicable the courts shall fix the advance on costs in an amount likely to cover the fees and expenses of the arbitrators and the ICC administrative expenses. The advance on costs fixed by the court shall be payable in equal shares by the claimant and the respondent. The amount of any advance on costs fixed by the court may be subject to readjustment at any time during the arbitration. In all cases any party shall be free to pay any other party's share of any advance costs should such other party fail to pay its share. Where a request for an advance on costs has not been complied with and after a consultation with the Arbitral Tribunal the Secretary General may direct the

Arbitral Tribunal to suspend its work and set a time limit which must not be less than 15 days on the expiry of which the relevant claims shall be considered as withdrawn.<sup>88</sup>

On 15 May 2013, ICC gave notice that having three arbitrators increased the Arbitral Tribunal's fees and expenses. It stated that based on the first defendant's claim valued at £100,000, the fee for a sole arbitrator was \$11,437 and the fee for three arbitrators would be \$34,311. It stated that if the parties agreed to have a sole arbitrator, the court should be notified as soon as possible.

After notice was given of a sole arbitrator the ICC issued a Notice stating that the Secretary General had readjusted the provision for advance on costs to \$11,000 taking in view of the choice of a sole arbitrator. The appellant had already paid 3,000 USD so there was a remaining balance of 8,000 USD to be paid.

On 7 November 2013, ICC issued a further notice wherein it noted the amount in dispute to be \$1.756m which included the appellant's £100,000 claim and respondent's £1.249m counterclaim. Consequently the fees due in respect of the arbitration increased to \$95,000 for which each party was liable to equal contribution. Thus the payment due by the appellant was \$36,500, having already paid £11,000 and respondent was due to pay \$47,500.

In a letter dated 17 January 2014, copied to the ICC, the respondent's solicitor indicated that 'it intended to proceed defending the appellant's claim through the arbitration proceedings but was not making a counterclaim in light of concern that any counterclaim would not be met by the appellant given its financial standing. This was repeated in correspondence of 1 August 2014 to the ICC.'<sup>89</sup>

The parties were dissatisfied with the amount of the arbitration fees. On 26 May 2014, ICC issued another Notice stating 'that the respondent had consistently refused to pay its share of the advance on costs and the ICC had invited the appellant to pay the outstanding share of the advance on costs in its entirety.'<sup>90</sup>

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<sup>88</sup> *Trunk Flooring* (n 87).

<sup>89</sup> *ibid.*

<sup>90</sup> *ibid.*

In a letter of 11 August 2014 the appellant wrote the ICC again on the issue of costs. It reiterated that the determination of its interest is a maximum of 100,000 euros and the sum demanded by ICC as advance cost, which is approximately 70,000 euros, is completely uneconomical in the circumstance. It stated further that the cost is arbitrary and unfair for both parties for economic reasons and the only benefiting party would be the ICC. It concluded the letter by by urging the ICC ‘ “... to reconsider the taxation of costs again and give the parties the opportunity to end the dispute reasonably.” ’<sup>91</sup>

Eventually, the ICC in a further correspondence, withdrew the claim on the following terms:

“Following claimant's objection to the application of Article 36(6) of the Rules, on 4 September 2014, the International Court of Arbitration of the International Chamber of Commerce (‘Court’) decided that the claims are considered withdrawn. Therefore, pursuant to Article 36(6) of the Rules, claimant's claims are considered withdrawn as of 12 August 2014, without prejudice to the reintroduction of the same claims in another arbitration ( *our emphasis* ).”<sup>92</sup>

Subsequent to the withdrawal of the claim by the ICC, the respondent went back to the Commercial Court for the stay granted in the proceedings to be lifted and the appellant opposed.

The learned judge in lifting the stay held as follows:

“The arbitration proceedings have been treated as withdrawn by the ICC by their recent letter to that effect. Neither party to the arbitration intends to proceed. The plaintiff and the second defendant are not now acting under the arbitration agreement. Both the plaintiff and the second defendant accept that the other party will not act under the arbitration agreement. The opportunity has been available for them to do so and they have allowed that opportunity to be withdrawn. The concept of abandonment ... applies in the circumstances of the present case. The parties have abandoned the arbitration agreement. That being so I am satisfied that

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<sup>91</sup> *ibid.*

<sup>92</sup> *ibid.*

on the ground of abandonment the agreement has become inoperative and the stay in the proceedings should be removed.”<sup>93</sup>

On appeal, the court of appeal had to determine whether the arbitration agreement had been abandoned by the parties and thus become inoperative. In determining the issue of abandonment the Court of Appeal noted that the learned judge ‘correctly invoked *Russell on Arbitration* 23rd Edition at paragraph 7.046 in setting out the basic three grounds on which a stay might not be granted’ to wit:

(a) The agreement is null and void where the arbitration agreement (as opposed to the matrix agreement) was never entered into or where it was entered into but subsequently has been found to have been void ab initio. (*No argument was made that this principle was applicable in the present case*).

(b) The agreement is inoperative where for example the arbitration agreement has been repudiated or abandoned or contained such an inherent contradiction that it could not be given effect.

(c) The arbitration agreement will be incapable of performance where, even if the parties were ready, willing and able to perform, the agreement could not be performed by them. Distinction must be drawn between a party being incapable of performing the agreement as opposed to the agreement being incapable of being performed. It is only the latter that renders the agreement incapable of performance. (See *Paczy v Haendlar and Natermann GmbH* [1981] 1 Lloyds Reports 302 ). Impecuniosity is not a circumstance of that kind.<sup>94</sup>

On determination of whether the arbitration agreement has been repudiated or abandoned, the Court of Appeal stated that there was no basis for concluding on an objective assessment of all the circumstances of the case that there has been an offer by one of the parties to abandon the arbitration aspect of the contract which has been accepted by the other and communicated to the offeror. Secondly the Court of Appeal distinguished between a termination of an arbitration

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<sup>93</sup> *ibid* para 31.

<sup>94</sup> *Trunk Flooring* (n 87) para 19.

reference and the termination of an arbitration agreement. It stated that the costs issue had led to the termination of the arbitration reference and the arbitration agreement is still valid.

The Court emphasised that ‘ICC expressly envisaged that the same claim could be reintroduced in another arbitration notwithstanding that the present reference had been withdrawn.’<sup>95</sup> This according to the Court ‘left the door open for further arbitration reference’.<sup>96</sup> Consequently, it was held that there was no basis upon which the stay can be refused on the grounds that the agreement to arbitrate has become inoperative or that the agreement to arbitrate has been abandoned and it was ordered that the stay be maintained.

### 3.2 The approach in US courts

In *Roldan v Callahan & Blaine*<sup>97</sup>, elderly plaintiffs of limited financial means were among a group of plaintiffs in an underlying litigation concerning toxic mold contamination in the apartment building where they were living. The plaintiffs relied on subsidies under a federal program providing financial assistance to low-income tenants. The plaintiffs were represented in the litigation by attorney Richard Quintilone and before commencement of trial, he informed them vide letter that he had associated Callahan as co-counsel in their case. He explained to them that Callahan’s has a high reputation in solving complex litigation cases and partnering with Callahan ‘“would serve as an invaluable opportunity to help bring forth meaningful settlement discussions . as well as assist in the substantial upcoming expert costs.”’<sup>98</sup> He referred the plaintiffs to Callahan’s retainer agreement, a 9 page document which contained an arbitration clause on its 8<sup>th</sup> page and the retainer agreement was signed by the plaintiffs.

According to complaints filed by plaintiffs, Quintilone and Callahan began pressuring the plaintiffs to settle the case on unfavorable terms. When the plaintiffs resisted, the attorneys sought to withdraw from their representation, and filed applications to have guardians ad litem appointed to take control of the plaintiffs' affairs on ground of ‘ “inability to assist counsel with the prosecution

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95 *Trunk Flooring* (n 87) para 36.

96 *ibid.*

97 219 Cal. App. 4th 87 (2013).

98 *ibid.*



of the case.”<sup>99</sup> The ‘[p]laintiffs were forced to incur the expense of an independent attorney and a psychiatrist to assist them in their successful defense of the motion for appointment of the guardians.’<sup>100</sup>

Eventually, the plaintiffs agreed to settle the case. The plaintiff’s subsequently alleged that: the sums the received were far less than the real value of the case; the attorneys failed to release their settlement proceeds on time; and that the attorneys refused to give them a copy of their file in the litigation case when requested to do so. The plaintiffs, thus, commenced proceedings against the attorneys in court for alleged misconduct, financial elder abuse, conversion, and breach of fiduciary duty, among others. Callahan and Quintilone filed petitions for orders compelling arbitration of the complaints against them.

The US statutory provision for stay of proceedings in respect of matters referable to arbitration is similar to that of the Arbitration Act 1996. Section 3 of the Federal Arbitration Act provides as follows:

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.<sup>101</sup>

The California Arbitration Act has similar provisions to section 3 of the FAA.<sup>102</sup> In oppositions to the petitions, the plaintiffs as part of their arguments, asserted that they were unable to afford the costs of arbitration. The trial court granted Callahan's petitions but denied Quintilone's petition on the basis that his retainer agreement did not contain a binding arbitration agreement. The court

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99 *ibid.*

100 *Roldan* (n 97).

101 9 U.S. Code § 3.

102 Code Civ. Proc., § 1281.2 & 1281.4.

ordered that the plaintiffs cases be consolidated into a single arbitration against Callahan and stayed the non-arbitrable claims against Quintilone pending determination of the Callahan arbitration.

The plaintiffs petitioned the court for writs of mandate overturning the court's orders enforcing Callahan's arbitration clause and the petitions were denied. In May 2012, the plaintiffs 'filed a joint motion in the superior court, seeking an order decreeing that they are not required to pay any portion of the "up front" cost of the arbitration between themselves and Callahan.'<sup>103</sup> They relied on an undisputed fact that they were indigent, and that circumstances had changed since orders compelling them to arbitrate were issued, as they have been subsequently declared as acting in forma pauperis by the court. In view of that circumstance, the plaintiffs claimed that 'requiring them to pay a portion of the "up front" arbitration fees effectively precluded them from pursuing their claims against Callahan in the arbitration forum.'<sup>104</sup> Callahan opposed the motion and also filed a motion seeking to dismiss the arbitration on the ground that the plaintiffs were not complying with their obligation to share in the cost of the arbitration.

Both motions were denied by the trial court. In regard to the plaintiffs' motion, the trial court held that:

[P]laintiffs' in forma pauperis status was irrelevant, because such a determination merely resulted in a "waiver of court charges," and "d[id] not impose a cost upon the opposing counsel." While the court acknowledged that arbitrators "[a]re, apparently, pretty expensive," it also noted "that's life outside this courtroom."<sup>105</sup>

The Californian Court of Appeal, Fourth District in reversing the order of the lower court held that:

If, as plaintiffs contend, they lack the means to share the cost of the arbitration, to rule otherwise might effectively deprive them of access to any forum for resolution of their claims against Callahan. We will not do that. Of course, as the trial court recognized, we cannot order the arbitration forum to waive its fees, as a court would do in the case of an indigent litigant. Nor do we have authority to order Callahan to pay plaintiffs' share of those

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103 *ibid* n 97

104 *ibid*

105 *ibid*

fees. What we can do, however, is give Callahan a choice: if the trial court determines that any of these plaintiffs is unable to share in the cost of the arbitration, Callahan can elect to either pay that plaintiff's share of the arbitration cost and remain in arbitration, or waive its right to arbitrate that plaintiff's claim.<sup>106</sup>

Although the court noted that there is a presumption that the plaintiffs understood the retainer agreement which they signed and that they would have to share in the cost of arbitration it stated that the 'Plaintiffs' presumed knowledge of the law does not afford any basis to conclude that they would have had any idea of just how much a pro rata share of those expenses and fees might be.<sup>107</sup> The choices presented by the court of appeal resonates with the outcome which the learned judge might have envisaged would happen when he stayed the proceedings in *Paczy*,<sup>108</sup> to wit whether the economically superior party who insisted on resolving the dispute by arbitration would elect to pay the cost of the arbitration or waive the contractual right to arbitrate and allow the matter to be heard by the court.

In *Tillman v Tillman*<sup>109</sup>, Renee Tillman's husband, Tim Tillman, died in a truck accident in 2002. She hired a law firm (Rheingold) to represent her. The firm filed a wrongful death suit against the manufacturer of the truck her husband was driving. Renee won the suit and was awarded about eight million USD, an amount which was later reduced on appeal.

Renee and Rheingold firm were later sued by Sean Tillman, the deceased's son from a previous marriage. Sean asserted that Renee and Rheingold firm wrongfully excluded him from the suit against the truck manufacturer and were thus negligent and in violation of a California requirement that an heir suing in a wrongful death action join all other known heirs. His claims against the Rheingold firm were dismissed but his action against Renee proceeded. Renee, in turn, filed a complaint against Rheingold firm, alleging that it committed malpractice by not including Sean in the wrongful death suit and by failing to advise her of the rights of her late husband's other heirs.

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<sup>106</sup> *ibid* n 97

<sup>107</sup> *ibid*.

<sup>108</sup> *Paczy* n 62.

<sup>109</sup> 825 F.3d 1069 (9th Cir. 2016).

In response to Renee’s complaint, the Rheingold firm filed a motion to compel arbitration relying on an arbitration clause in its retainer agreement with Renee. The court granted the motion to compel arbitration and stayed proceedings. Both parties began arbitration under the rules of the American Arbitration Association (“AAA”), as provided in the retainer agreement.

During the arbitration proceedings, Renee objected to several aspects of the arbitration as ‘unnecessarily increasing costs’.<sup>110</sup> She particularly challenged ‘the need for the arbitration to include a “case-within-a-case” adjudication, in which the arbitrator would rehear witnesses and evidence presented in the underlying wrongful death action.’<sup>111</sup> The arbitrator nonetheless scheduled additional dates for a case-within-a-case adjudication. ‘Renee borrowed money, and her counsel in the arbitration proceedings agreed to front certain costs.’<sup>112</sup> Nevertheless, she was ultimately unable to provide an 18,562.50 USD deposit which the AAA demanded as a condition of continuing the proceedings.

The AAA ‘then “inquir[ed] as to whether [the firm was] willing to cover th[e] deposit,” but the firm declined’<sup>113</sup>. Renee requested that the AAA require the firm to pay the deposits going forward, under AAA rules authorizing interim relief and the arbitrator responded that ‘it did “not intend to decide the motion for interim relief” until the deposits had been paid.’<sup>114</sup> The AAA subsequently set a deadline for Renee to submit the funds and eventually terminated the arbitration proceedings due to the unpaid deposits.

Rheingold firm subsequently went back to the district court with a motion that the stay be lifted and that the suit be dismissed because of Renee’s failure to pay the deposits, which according to the firm, was a violation of the court’s order compelling arbitration. Renee objected, arguing that ‘she had fully participated in the arbitration and done “everything in her power” to proceed before the arbitrator.’<sup>115</sup> She argued further that the firm was also at fault for the termination of the arbitration proceedings, because, under the AAA rules, it could have paid to continue the arbitration proceedings but elected not to pay.

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<sup>110</sup> *Tillman* (n 109).

<sup>111</sup> *ibid*.

<sup>112</sup> *ibid*.

<sup>113</sup> *ibid*.

<sup>114</sup> *ibid*.

<sup>115</sup> *ibid*.

Before ruling on the motion, the district court allowed Renee to adduce evidence to show that she could not pay her share of the arbitration fees because of her financial situation. This she did by submitting a declaration with various exhibits showing how the money awarded from the initial settlement had been exhausted. After reviewing the evidence, the district court found that Renee was truly “unable to pay for her share of arbitration.” The court, thus, declined to dismiss her case on that basis and instructed the parties to further brief it on the issue of how to proceed given Renee’s inability to pay the fees.

The district court eventually dismissed the case on the basis that the AAA’s rules required the parties to bear the costs of arbitration equally and allowed the arbitrator to suspend the proceedings. Section 1 of the Federal Arbitration Act also deprived it of ‘authority to hear “the claims that would have been subject to the arbitration agreement,” and dismissal was required.’<sup>116</sup> Renee appealed the decision of the district court.

On appeal, the US Court of Appeals, Ninth District, affirmed the district court’s lift of the stay but held that the district court erred in dismissing the suit. The Court of Appeal noted that ‘The FAA requires courts to stay court proceedings on issues subject to arbitration “until such arbitration has been had in accordance with the terms of the agreement.”’<sup>117</sup> The Court of Appeal then considered what it means for ‘an arbitration to “ha[ve] been had in accordance with the terms of the agreement”?’ The Court of Appeal interpreted arbitration as being ‘had’ in the context of section 3 of the FAA to mean that ‘the parties engaged in arbitration until the arbitrator terminated those proceedings.’<sup>118</sup> The arbitration was terminated because Tillman could no longer pay the arbitrator’s fee and the arbitrator did not enter any sort of award or judgment.

The Court of Appeal, citing its earlier decision in *Ferdik v Bonzelet*, stated that, generally, ‘the “harsh penalty” of dismissal “should only be imposed in extreme circumstances.”’<sup>119</sup> The Court noted that the ‘district court reviewed Tillman’s submissions and concluded that she did lack the resources to make the requested arbitration deposit and stated that ‘Whether Tillman “fail[ed] . . . to

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<sup>116</sup> *ibid.*

<sup>117</sup> *ibid.*

<sup>118</sup> *ibid.*

<sup>119</sup> 963 F.2d 1258, 1260 (9th Cir. 1992).

comply with . . . [the] court order” to arbitrate is debatable, as she was willing to arbitrate but unable to pay for it, and the Rheingold firm could have fronted the costs but did not.’<sup>120</sup> The Court stated that such failure to comply was not culpable and does not merit a harsh penalty in view of ‘the public policy favouring disposition of cases on their merits.’<sup>121</sup> The Court held further that as the arbitration proceedings terminated before the merits were reached or any award issued, allowing Renee’s case to proceed in district court is the only way her claims will be adjudicated.

The Court of Appeal in its ruling recognised the importance of the policy of compelling arbitration in regard to an agreement to arbitrate. The Court stated that its ruling, which allows Renee’s case against the Rheingold firm to proceed in the court despite the existence of an arbitration agreement between the two, does not run afoul of that policy. The Court stated that the decision that Renee’s case may proceed does not mean that parties may refuse to arbitrate by deciding not to pay for arbitration. ‘If Tillman had refused to pay for arbitration despite having the capacity to do so, the district court probably could still have sought to compel arbitration under the FAA’s provision allowing such an order in the event of a party’s “failure, neglect, or refusal” to arbitrate.’<sup>122</sup>

Again In *Rae Weiler v Marcus & Millichap Real Estate Investment Services, Inc.*,<sup>123</sup> the Californian Court of Appeal had to determine a case involving the impecuniosity of a party. The plaintiff and her husband, both in their 80’s, were affluent at some point in their lives. Part of their assets included two properties in Las Vegas, Nevada. In 2006, they exchanged the Las Vegas properties, under US federal Internal Revenue Code, for a commercial property in Texas which was supposedly worth 4.1 million USD. The defendants represented the plaintiff and her husband in the property exchange transactions and the relevant contracts which the plaintiff and her husband signed with the defendants contained arbitration clauses.

When Texas commercial property was acquired, the plaintiff and her husband believed that they would receive rent payments from a tenant who operated a restaurant business there. They also understood that the tenant had an obligation to pay the property taxes under an existing lease. Some

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<sup>120</sup> *Tillman* (n 109).

<sup>121</sup> *ibid*, citation omitted.

<sup>122</sup> *ibid*.

<sup>123</sup> 2018 WL 2011048 (Cal. Ct. App. 4th Dist. no. G053953 (Apr. 30, 2018)).

time thereafter, the tenant became delinquent in making rent payments and defaulted in payment of the property taxes. This went on for the next seven years consequently leading to an alleged loss to the plaintiff and her husband of more than \$600,000 in income. They eventually sold the property for \$2.1 million less what they paid for it.

Before selling the property at a loss, the plaintiff filed a suit against the defendants for breach of breach of fiduciary duty amongst others, and sought compensatory and punitive damages. It was the plaintiff's assertion in the suit that she had informed the defendants that 'she knew very little about commercial real estate investing . . . and that she wanted a safe and secure investment with a decent return.'<sup>124</sup> It was also alleged that the 'defendants recommended the Texas property because it was a "wonderful investment" and the restaurant on the property "was busy and doing well financially."'”<sup>125</sup>

The defendants filed a motion, to which the plaintiff did not oppose, to compel arbitration. The plaintiff was subsequently ordered to pursue her claims by arbitration to be administered by the American Arbitration Association and she commenced an arbitration proceedings against the defendants.

Over the course of about two years that followed, the arbitration proceedings moved slowly due to disagreements between the parties about the substance of plaintiff's claims and about how the arbitration should proceed. In particular, due to the amount of the plaintiff's claim (2.8 million USD) the defendants insisted that pursuant to the AAA rules, the case could ' "*only be heard and determined by a Panel of three arbitrators.*" '”<sup>126</sup> The plaintiff, on the other hand argued that a single arbitrator was permissible and appropriate and an arbitrator eventually ordered that the case should be decided by a panel of 3 arbitrators at an hourly rate of 1,450 USD.

Close to three years after the court ordered the arbitration, and during a second prehearing conference with the arbitrators, the plaintiff asserted she was unable to afford her 50-percent contribution of the arbitration costs. At that time, the plaintiff's share of the arbitration costs had already exceeded 15,000 USD, and she anticipated the overall costs to complete the arbitration

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<sup>124</sup> *ibid*/

<sup>125</sup> *ibid*.

<sup>126</sup> *Weiler* (n 123).

would be in excess of 100,000 USD, excluding the costs of expert witness and discovery related fees. Consequently, the Plaintiff sought the *Roldan* relief from the arbitrators, to wit that the arbitrators should issue an order giving the defendants two options: ‘continue with the arbitration and pay cost of it; or allow the matter to be tried in court’.<sup>127</sup> The arbitrators ruled that it was outside their jurisdiction and directed the plaintiff to court. Consequently, the plaintiff sought the said reliefs in the court. She asserted that she could no longer afford the arbitration proceedings. The plaintiff asserted that, if she were to remain in arbitration and pay half of the arbitration costs which was in excess of 100,000 USD, she would be unable to pursue her claims at all.

The court granted summary judgment to the defendants on the grounds that the arbitration provisions were valid and enforceable, and that the plaintiff’s alleged inability to pay the anticipated arbitration costs was irrelevant. On appeal, the Californian Court of Appeal held that the lower court erred in granting the defendants’ motion for summary judgement. In so holding the it stated that:

Though the law has great respect for the enforcement of valid arbitration provisions, in some situations those interests must cede to an even greater, unwavering interest on which our country was founded—justice for all. Consistent with *Roldan*, and federal and California arbitration statutes, a party’s fundamental right to a forum she or he can afford may outweigh another party’s contractual right to arbitrate.<sup>128</sup>

The Court of Appeal made an astute observation that:

The very reason plaintiff filed the underlying court action against defendants is because their alleged wrongful acts led her and her husband to lose a significant amount of money. And, in the many years of pursuing her case in arbitration, it appears defendants’ tactical decisions have further contributed to plaintiff’s ostensible financial ruin. In other words, defendants appear to have effectively hindered plaintiff’s continued performance under the arbitration provisions.

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<sup>127</sup> *ibid.*

<sup>128</sup> *ibid.*



A significant fact worthy of note is that the defendants said ‘ostensible financial ruin’ of the plaintiff occurred due to how the defendants were able to wield the rules of the arbitration in a way which consequently weakened the financial ability of the claimant and consequently her ability to prosecute her claims.

Dissatisfied with the decision of the Court of Appeal, the defendants appealed to the Supreme Court of the United States as petitioners in *Marcus & Millichap Real Estate v. Rae Weiler*<sup>129</sup>. One of the issues determined by the Supreme Court was ‘ “whether the FAA preempts a state rule that denies enforcement of a cost-sharing provision of an arbitration agreement without finding that the provision violates a general principle of state contract law.” ’<sup>130</sup> In determination of the issue the Supreme Court noted that the briefing in the Court of Appeal indicated that both parties agreed to subject their arbitration agreement to California arbitration law and litigated in the Court of Appeal according to that belief.

The Supreme Court stated further that both parties agreement to abide by state law in respect of arbitration procedures means in effect that, ‘even if the FAA would not itself incorporate the state-law rule applied below concerning allocation of fees, it does not preempt a state court from applying that rule’.<sup>131</sup>

Although, the Supreme Court declined to entertain jurisdiction of the appeal on several grounds, it stated that the decision would not merit review in any event because it was not in conflict with any of its past decisions or that of any other court and was not erroneous in any respect.<sup>132</sup>

The decisions of the Californian Court of Appeal, Fourth District, in *Roldan*<sup>133</sup> and *Weiler*<sup>134</sup> were influenced by ‘ “California’s long-standing public policy of ensuring that all litigants have access to

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129 No. 18-929.

130 *ibid* .

131 *ibid*.

132 *ibid*.

133 *Roldan* (n 97).

134 *Weiler* (n 123).

the justice system for resolution of their grievances, without regard to their financial means.”<sup>135</sup>

What this means in essence is that an arbitral award emanating from England, for instance where a party has been foreclosed from prosecuting his claim due to impecuniosity, might be challenged on the ground of public policy if enforcement is sought in the US state of California.

## **4 How can the financial impacts of procedural due process conformity on economically inferior parties be mitigated?**

The purpose of due process is to ensure a fair means of resolution of matters arising in arbitration proceedings. In view of the dominance of arbitration in resolution of commercial disputes, it is essential to ensure its efficiency. Justice cannot be sacrificed for efficiency so the requirement of due process cannot be removed from arbitration. However mitigation of the financial impact of procedural due process conformity and potential abuse of due process might be achieved in the following ways:

### **4.1 Costs to follow the event**

One way is for arbitrators, to adhere strictly to the costs follows the event principle such that a party who makes an unsuccessful application during proceedings would be obliged to pay cost upon the determination of the application. This is achievable pursuant to Section 61 of the Arbitration Act which provides that ‘[u]nless the parties otherwise agree, the tribunal shall award costs on the general principle that costs should follow the event except where it appears to the tribunal that in the circumstances this is not appropriate in relation to the whole or part of the costs.’<sup>136</sup> Adherence to this principle would serve as a deterrence for parties in making frivolous applications during proceedings.

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<sup>135</sup> *ibid.*

<sup>136</sup> Arbitration Act 1996.

With the aim of preventing dilatory tactics by parties, some institutional rules provides that arbitrators can allocate costs based on a parties' conducts. An example is Article 28.4 of the LCIA rules which provides that:

The Arbitral Tribunal shall make its decisions on both Arbitration Costs and Legal Costs on the general principle that costs should reflect the parties' relative success and failure in the award or arbitration or under different issues, except where it appears to the Arbitral Tribunal that in the circumstances the application of such a general principle would be inappropriate under the Arbitration Agreement or otherwise. The Arbitral Tribunal may also take into account the parties' conduct in the arbitration, including any co-operation in facilitating the proceedings as to time and cost and any non- co-operation resulting in undue delay and unnecessary expense. Any decision on costs by the Arbitral Tribunal shall be made with reasons in the award containing such decision.<sup>137</sup>

The problem with the above provision is that, a party may disagree to settle in some cases where the offer for settlement is made by a financially superior party who engaged in activities that are calculated to frustrate the financially inferior party out of the proceedings. Where such offer is rejected and the financially inferior party loses the case in the end, his failure to accept the settlement offer might be prejudicial to him in the determination of costs after the proceedings.

Costs in proceedings are usually awarded in cause whereas costs ought to follow the event to deter activities that might frustrate proceedings. Where costs are made in cause, costs would be awarded to the winning party at the end of the arbitration proceedings. Where on the other hand, costs follow the event, order of cost could be made immediately after the hearing of an interlocutory application in favour of a successful party in the hearing of the application.

## **4.2 Allocation of costs between unequal parties**

Parties could agree on how costs should be paid in the event that one party becomes unable to pay its contribution to the costs of arbitration. Parties usually have the autonomy to agree on the method

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<sup>137</sup> London Court of International Arbitration 'Arbitration Rules' (2014)

<[http://www.lcia.org/Dispute\\_Resolution\\_Services/lcia-arbitration-rules-2014.aspx](http://www.lcia.org/Dispute_Resolution_Services/lcia-arbitration-rules-2014.aspx)> accessed 1 May 2017

of allocating the costs of arbitration between themselves subject to limitations under national law.<sup>138</sup> Although, ‘specific pre-dispute agreements on the allocation of costs are rare. In some jurisdictions, they may be used in contracts between unequal parties.’<sup>139</sup> For instance, ‘in Finland, managing director agreements sometimes provide that, in the event of a dispute, any resulting arbitration costs shall be borne solely by the economically superior party (i.e., the company that is the managing director’s employer) regardless of the outcome of the dispute.’<sup>140</sup> Such agreement would prevent the economically superior party from engaging in activities that are calculated to financially exhaust the economically inferior party. However, pursuant to section 60 of the Arbitration Act, this sort of agreement can only be valid if it was made after the dispute arose.

Pursuant to section 63 (1) of the Arbitration Act,<sup>141</sup> parties are free to agree as to what costs are recoverable. Thus to eliminate the disparity between unequal parties in regard to financial strength, parties could agree, prior to disputes, that legal fees of legal representatives shall be recoverable either partly or in full. Absent such agreement, the tribunal may also use its discretion, where possible under a relevant institutional rule, to award the costs incurred by parties for legal presentation. For instance, Article 28.3 of the LCIA rules gives the tribunal power to decide by an award, on such reasonable ground basis as it thinks fit, that all or part of the legal or other expenses incurred by a party (the “Legal Costs”) be paid by another party.<sup>142</sup> Article 28.3 further provides that ‘[t]he Arbitral Tribunal shall not be required to apply the rates or procedures for assessing such costs practised by any state court or other legal authority.’<sup>143</sup>

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138 Mika Savola, ‘Awarding Costs in International Commercial Arbitration’, article in the Scandinavian Studies in Law, Vol. 63, 2017.

139 *ibid.*

140 *ibid.*

141 London Court of International Arbitration ‘Arbitration Rules’ (2014)

<[http://www.lcia.org/Dispute\\_Resolution\\_Services/lcia-arbitration-rules-2014.aspx](http://www.lcia.org/Dispute_Resolution_Services/lcia-arbitration-rules-2014.aspx)> accessed 1 May 2017.

142 *ibid.*

143 *ibid.*

## 5 Conclusion

The first and second research questions posed in this thesis can be answered in the affirmative: conformity with the requirements of procedural due process can increase the costs of arbitration proceedings and economically superior parties, armed with this knowledge, can cleverly wield procedural due process conformity effectively as an oppressive tool to frustrate economically inferior parties in arbitration proceedings. Such conduct, on the part of an economically superior party can result in procedural due process having a counterproductive impact on the objective of arbitration under the Arbitration Act, to wit the attainment of fair resolution of dispute without unnecessary delay and expense.<sup>144</sup>

In regard to the third research question, the approach of the UK courts means that a party who becomes impecunious and unable to pay for the costs of arbitration would be foreclosed from obtaining justice through neither arbitration nor litigation. In the UK courts, strong emphasis is placed on the validity of an existing arbitration agreement between the parties. Thus, as long as there is an existing valid arbitration agreement, the courts are unlikely to lift a stay of the proceedings even if any of the party is unable to afford the costs of arbitration. The consequent result of this approach is that where a party purposely makes arbitration expensive in order to frustrate an economically inferior party in the prosecution of its case, there is no remedy available in the UK courts. Impecuniosity of a party could thus prevent the attainment of arbitral justice and access to justice in the national courts by virtue of parties' agreement to arbitrate.

The approach in the US courts is more pragmatic. Rather than placing emphasis on the existence of a valid arbitration agreement and whether to invalidate same due to the impecuniosity of a party and its inability to pay for arbitration, the courts leave open the options to either continue arbitration or resort to litigation. A stay of proceedings could thus be lifted, despite the existence of a valid agreement to arbitrate, if an economically inferior party lacks the wherewithal to pay for the cost of arbitration and an economically superior party is unwilling to pay for the party's share of the arbitration costs. The Supreme Court in *Weiler* case in a well considered ruling reiterated the fact that Ms. Weiler abided by the arbitration agreement to the best of her ability and was not unwilling to continue arbitrating, but she could not continue to pay the costs of arbitration.<sup>145</sup>

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<sup>144</sup> Arbitration Act 1996, s 1(b).

<sup>145</sup> 2018 WL 2011048 (Cal. Ct. App. 4th Dist. no. G053953 (Apr. 30, 2018)).

When parties enter into contracts such as construction contract for instance, the financial strength of the contractee would often be an incentive to the contractor in making the contract. It is when the contractee defaults in its obligation under the contract that its financial prowess becomes capable of being wielded as an oppressive tool.

*Ubi jus ibi remedium* (where there is a wrong there is a remedy) is one of the fundamental principles of law. Although, the English court in *Paczy* expressed sympathy towards the plaintiff, yet they could not help his case due to their approach to interpretation of the statute. The US court on the other hand expressed its cognisance of the fact that a party accused of wrongdoing could ensure that a dispute in respect of the alleged wrongdoing is arbitrated and tactfully make the proceedings so expensive such that the other party would have no choice but to give up. The approach of the US court, thus, ensures that ‘those compelled to arbitrate will not, as a result, be inherently disadvantaged.’<sup>146</sup>

Perhaps the UK courts did not envisage the scenarios which occurred in the US cases, to wit the possibility that one party could tactfully make an arbitration proceeding expensive for the other party. It is hoped that in future decisions, the learned judges of the UK, by considering the said scenarios, would advert their minds to the plights of impecunious parties in the pursuit of arbitral justice.

The section 1(b) of the arbitration Act provides that ‘[T]he parties should be free to agree how their disputes are resolved, subject only to such safeguards as are necessary in the public interest’. The section thus, in essence, gives courts the power to exercise discretion in applying safeguards in the public interest. One of such safeguards is arguably access to justice in the national court when a party becomes unable to obtain arbitral justice due to impecuniosity. Bearing in mind that a party’s impecuniosity might be caused by several circumstances which might not be attributable to another party with whom an agreement to arbitrate had been made, the decision to allow a party to resort to litigation could be made based on the merits of individual cases.

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146 *ibid.*